

October 4, 2010

INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and
Members of the City Commission
City of Adrian, Michigan

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Adrian, Michigan, as of and for the year ended June 30, 2010, which collectively comprise the City's basic financial statements as listed in the table of contents. We have also audited each nonmajor governmental fund and internal service fund, each nonmajor enterprise fund, and the fiduciary fund type presented in the accompanying combining and individual fund financial statements and schedules, also individual fund statements for discretely presented component units; and schedules of indebtedness of the City of Adrian, Michigan, as of and for the year ended June 30, 2010, as listed in the table of contents. These financial statements are the responsibility of the City of Adrian, Michigan's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Adrian, Michigan, as of June 30, 2010, and the respective changes in financial position and cash flows, where applicable, thereof and the budgetary comparison for the all major governmental funds for the year then ended in conformity with accounting principles generally accepted in the United States of America.

October 4, 2010

To the Honorable Mayor and
Members of the City Commission
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In addition, in our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of each nonmajor governmental and internal service funds nonmajor enterprise fund, and fiduciary fund type of the City of Adrian as of June 30, 2010, and the respective changes in the financial position and cash flows, where applicable, thereof and the budgetary comparison for all nonmajor governmental funds, and includes the individual fund statements for discretely presented component units and schedules of indebtedness for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 4, 2010 on our consideration of the City of Adrian, Michigan's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in conjunction with this report in considering the results of our audit.

The management's discussion and analysis and pension plan schedule on pages 39 through 53 and page 107, is not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Adrian, Michigan's basic financial statements. The introductory section, and statistical tables are presented for purposes of additional analysis and are not a required part of the basic financial statements. The introductory section and statistical tables have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements of the City of Adrian, Michigan. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Robertson, Eaton & Owen, P.C.

CITY OF ADRIAN, MICHIGAN
COMPREHENSIVE ANNUAL FINANCIAL STATEMENT
Management's Discussion and Analysis
November 1, 2010

As management of the City of Adrian, we offer readers of the City of Adrian's financial statements this narrative overview and analysis of the financial activities of the City of Adrian for the fiscal year ended June 30, 2010. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our letter of transmittal, which can be found on pages 1-33 of this report. All amounts, unless otherwise indicated, are presented in whole dollars.

Financial Highlights

- The Assets of the City of Adrian exceeded its liabilities at the close of the most recent fiscal year by \$69,435,564 (*net assets*). Of this amount, \$6,184,155 (*unrestricted net assets*) may be used to meet the City's ongoing obligations to citizens and creditors.

The City's total net assets increased by \$1,492,243, a \$564,478 increase in Governmental Activities, and a \$927,765 increase in Business-Type Activities. The primary contributing factors relating to the increase in Net Assets for Governmental Activities are the renovation of the vacated and previously acquired Bank of Lenawee building for new City Hall (\$.4 million), the renovation of Adrian Public Library (\$1.4 million), the construction of a new Police Facility (\$2.1 million), and renovation of the previously acquired Adrian Public Schools Adult Education Center for the new City Commission Chambers (\$.4 million). Liabilities, on the other hand, reflected the issuance of \$7,040,000 in Limited Tax General Obligation Bonds to finance the foregoing projects, as well as consolidate all other outstanding General Obligation Debt. In addition, a grant funded conversion of one-way to two-way vehicular traffic system in downtown resulted in a \$1.4 million increase in infrastructure, primarily the ownership transfer of state roads to local control, as well as the addition of new traffic signals.

The primary reason for the overall increase in net assets in Business-Related Activities is the decrease in Noncurrent Liabilities due to the annual debt retirement related to outstanding low-interest revenue bonds issued through the State Department of Treasury Drinking Water and Sewer Revolving Loan Program. These loans were incurred for the purpose of developing the West-Side Well Field project, which provides an alternative ground water resource to the City's potable drinking-water system, improvements to the Water and Wastewater Plants, as well as the Water Distribution System and the Wastewater Collection System.

- As of the close of the current fiscal year, the City of Adrian's governmental funds reported combined ending fund balances of \$7,266,805, a decrease of \$1,573,096 in comparison with the prior year. Following is a summary of Net Change in Fund Balance for selected Funds:

General Fund	\$(1,253,589)
Major Street Fund	116,753
Local Street Fund	277,074
All Other	<u>(713,334)</u>
Total	<u><u>\$(1,573,096)</u></u>

The unfavorability for the General Fund is primarily due to the planned draw on Fund Balance in the amount of \$1,250,000 for the purpose of providing local matching funds to finance the

Downtown Government Complex. The increase in the Major Street Fund is due to the increased in encumbered funds attributable to the new anticipated construction of a new pedestrian bridge and pathway in Riverside Park. The increase in Local Street Fund reflects the \$414,000 due from the Municipal Street Fund tax levy for local street improvements; the coincident increase in liabilities reflects in the Municipal Street Fund.

Although not required to until the end of the FY2010-11 reporting period, the City of Adrian chose to implement the Governmental Accounting Standards Board (GASB) Statement No. 54 *Fund Balance* Reporting with the FY2008-09 Comprehensive Annual Financial Report. This important new standard has left unchanged the total amount reported as *fund balance*, but has substantially altered the categories and terminology used to describe its components. The new categories and terminology focus, not on financial resources available for appropriation, but on “the extent to which the government is bound to honor constraints on the specific purposes for which amounts in the fund balance can be spent.”

In compliance with Statement No. 54, financial statements for governmental funds report up to five (5) components of fund balance:

NON-SPENDABLE FUND BALANCE

Some of the assets reported in governmental funds are inherently non-spendable from the vantage point of the current period, including:

- Assets that will never convert to cash (e.g., prepaid items and inventories of supplies);
- Assets that will not convert to cash soon enough to affect the current period (e.g., the long-term portion of loans receivable and non-financial assets held for resale, such as foreclosure properties);
- Resources that must be maintained intact pursuant to legal or contractual requirements (e.g., the principal of an endowment or the capital of a revolving loan fund).

RESTRICTED FUND BALANCE

This describes the portion of fund balance that reflects resources that are subject to externally enforceable legal restrictions. Such restrictions are imposed by the government’s charter but most restrictions are typically imposed by parties altogether outside the governmental unit, by:

- Creditors (e.g., through debt covenants);
- Grantors;
- Donors or Contributors; and
- Other governmental units (e.g., through laws and regulations).

Restrictions also can arise when the authorization to raise revenues is conditioned upon the revenue being used for a particular purpose (e.g., gasoline taxes restricted for use for road repair or construction).

COMMITTED FUND BALANCE

Reflects the portion of fund balance that represents resources whose use is constrained by limitations that the government imposes upon itself at its highest level of decision-making (normally the City Commission) and that remain binding unless removed in the same manner. Resources accumulated pursuant to Stabilization Arrangements (e.g., rainy day funds or contingency funds) are reported in this category.

ASSIGNED FUND BALANCE

Describes that portion of fund balance that reflects a government's intended use of resources (previously referred to as Designated Fund Balance). Such intent would have to be established at either the highest level of decision-making (i.e., City Commission) or delegated to an appropriate designated official (i.e., City Administrator). It is the assigned fund balance category, too, that is used to reflect the appropriation of a portion of existing fund balance to eliminate a projected deficit in the subsequent year's budget.

UNASSIGNED FUND BALANCE

The General Fund, as the principal operating fund of the government, often will have resources in excess of what can be properly classified in one of the four categories already described. If so, that surplus is presented as *unassigned fund balance*.

If resources were not at least assigned, they could not properly be reported in a fund other than the General Fund. Therefore, only the General Fund can report a positive amount of *unassigned fund balance*. Conversely, any governmental fund in a deficit position could report a negative amount of as *unassigned fund balance*.

- At the end of the current fiscal year, total fund balance for the general fund was \$3,359,806 or thirty-five (30%) percent of budgeted general fund expenditures for FY2010-11. Of this amount, \$181,966 is considered Nonspendable and earmarked for inventories and pre-paid insurance. In addition, \$1,464,996 is Assigned for encumbrances and \$646,000 is designated by management for the following specific projects, leaving \$1,066,844 in Unassigned Fund Balance. The designations are detailed as follows:

1) Office Space Rental Program	\$545,000
2) Property Acquisitions, Demolitions and Options	50,000
5) Bohn Pool Analysis	26,000
6) Local Grant Match	<u>25,000</u>
Total	<u>\$646,000</u>

- The City of Adrian's total Long-Term Liabilities increased by \$2,281,241 or seven (7%) percent during the current fiscal year to a total of \$34,351,118. General Obligation Debt increased \$3,403,121, from \$4,272,752 to \$7,675,873. Consistent with the City's Capital Improvement Program, which addressed the need to replace the old City Hall and relocate the Police Department, funding was primarily derived from the Federal stimulus program through the issuance of Build America Bonds and Recovery Zone Economic Development Bonds that provided for a 35% and 45% rebate on annual interest payments. By taking advantage of provision of the federal American Recovery and Reinvestment Act (ARRA) of 2009, the City of Adrian will realize over a \$6.0 million interest savings over 25 years having issued a series of bonds totaling \$7,040,000 in November, 2009, to fund the new downtown City government complex, as well as consolidate all outstanding general obligation debt, including the following:

Series A - \$1,540,000 – Traditional Non-Taxable Limited General Obligation Bonds,
Series B - \$1,600,000 – Federally Taxable Build America Bonds (35% Interest Rebate), and
Series C - \$3,900,000 – Federally Taxable – Recovery Zone Economic Development Bonds (45% Interest Rebate).

Accessing this source of funding made the Downtown Government Complex affordable by spreading the cost over a 25-year time span, resulting in an annual incremental cost equivalent to only \$20 per household, while holding taxes unchanged.

The single most significant factor affecting FY2009-10 financial operations was incorporation of the \$7.1 million Build America bond issue to underwrite the cost of the Downtown Government Complex, including acquisition and renovation of a new City Hall and Commissioner Chambers, renovation of the Adrian Public Library and construction of a new Police Facility. The FY2009-10 Budget contemplated a planned draw of \$2,250,000 on General Fund-Fund Balance to provide an infusion of pay-as-you-go financing in order to reduce the need for additional debt financing. Approximately \$680,000 remains unspent as of June 30 and has been carried forward into the FY2010-11 Budget to complete the project, including demolition of the old City Hall, reconstruction of the South Toledo Street Parking Lot and installation of a new roof on the new City Hall.

In addition to funding the Downtown Government Complex, bond proceeds were utilized to consolidate all outstanding General Obligation debt, including:

<u>Description</u>	<u>Amount</u>
Parks & Forestry Facility	\$1,543,239
City Hall Land Contract	1,333,161
Police Department – Land and Bldgs.	503,378
Marvin Farm	542,790
Taxi Cab Building	<u>112,872</u>
Total	<u>\$4,035,440</u>

At a low net interest rate of 3.71%, afforded by the U.S. Treasury rebate program under the authority of the American Reinvestment and Recovery Act of 2009, the total savings (compared to traditional municipal debt financing) that will accrue to City of Adrian taxpayers over the 25-year life of the bond issue will amount to over \$6 million.

- Outstanding Revenue Bond Debt decreased by \$1,169,103, from \$27,012,358 to \$25,843,255; a summary follows:

<u>Purpose</u>	<u>Date of Issue</u>	<u>Total Amount</u>	<u>Interest Rate</u>	<u>Maturity Date</u>	<u>Outstanding Balance</u>
Wastewater System Improvements	09/26/02	\$ 8,920,000	2.500%	10/01/23	\$ 6,695,000
Water System Improvements	09/26/02	5,665,000	2.500%	10/01/23	4,250,000
Wastewater System Improvements	09/22/05	1,993,885	1.625%	04/01/27	1,728,885
Wastewater System Improvements	12/15/05	7,090,000	1.625%	04/01/27	6,047,663
Water System Improvements	09/27/07	<u>7,890,000</u>	2.125%	04/01/28	<u>7,121,707</u>
Total		<u>\$31,558,885</u>			<u>\$25,843,255</u>

Overview of the Financial Statements

These discussion and analysis are intended to serve as an introduction to the City of Adrian's basic financial statements. The City of Adrian's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

Government-wide Financial Statements. The *government-wide financial statements* are designed to provide readers with a broad overview of the City of Adrian's finances, in a manner similar to private-sector business.

The *Statement of Net Assets* (Pages 56-57) presents information on all of the City of Adrian's assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City of Adrian is improving or deteriorating.

The *Statement of Activities* (Pages 58-59) presents information showing how the City's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions of the City of Adrian that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*). The governmental activities of the City of Adrian include general government, public safety, highways and streets, sanitation, economic development, and culture and recreation. The business-type activities of the City of Adrian include water and sewer operations, storm water utility and automobile parking activities, as well as Dial-A-Ride Transportation.

The government-wide financial statements include not only the City of Adrian itself (known as the *primary government*), but also a legally separate Downtown Development Authority, a legally separate Local Development Finance Authority and a legally separate Brownfield Redevelopment Authority, for which the City of Adrian is financially accountable. Financial information for these *component units* is reported separately from the financial information presented for the primary government itself. The Dial-A-Ride transportation system and OMNI drug enforcement unit function, as well as the Internal Service Funds for Information Technology and Fire Department Motor Pool, for all practical purposes are departments of the City of Adrian and, therefore, have been included as an integral part of the primary government. The government-wide financial statements can be found on pages 56-59 of this report.

Fund Financial Statements. A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City of Adrian, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City of Adrian can be divided into three categories: governmental funds, proprietary funds and fiduciary funds.

Governmental Funds. Governmental funds are used to account for essentially the same functions reported as *governmental activities* in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures and changes in fund balances provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

The City of Adrian maintains twelve (12) individual governmental funds, including two (2) Internal Service Funds, Information Technology Fund and Motor Vehicle Pool Fund. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures and changes in fund balances for the general fund, major streets and local street funds, and the Fee Estate Fund, all four of which are considered to be major funds. Data from the other eight (8) governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these non-major governmental funds is provided in the form of *combining statements* elsewhere in this report. The basic governmental fund statements can be found on pages 60-62 of this report.

The City of Adrian adopts an annual appropriated budget for its general fund. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget (reference pages 64-69).

Proprietary Funds. There are traditionally two different types of proprietary funds. *Enterprise funds* are used to report the same functions presented as *business-type activities* in the government-wide financial statements. The City of Adrian uses enterprise funds to account for its water and sewer operations and for the Automobile Parking and Dial-A-Ride Systems, as well as the Capital Projects Revolving Fund and Storm Water Utility Fund. *Internal service funds* are an accounting device normally used to accumulate and allocate costs internally among the City of Adrian's various functions. The Information Technology Fund was established with the implementation of the FY2004-05 Budget and the Motor Vehicle Pool Fund was established with the implementation of the FY2007-08 Budget and expanded in the FY2008-09 Budget to encompass Police, DPW, Parks & Recreation, Inspection, Cemetery and City Engineer vehicles (reference pages 147-155). The FY2008-09 Budget established the Local Development Finance Authority Fund, which will be replacing the expiring LDFA Debt Fund, previously established to track captured revenue and debt repayment for the Garden State Tanning industrial facility. The final payment was made in June, 2008. The new Fund will derive its initial funding and assets from the dissolution of the Greater Adrian Industrial Development Corporation (GAIDC), which was originally created to promote industrial growth in the Greater Adrian area. The new LDFA is expected to continue and expand upon the efforts initiated by the GAIDC.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the Water System and the Wastewater System, both of which are considered to be major funds of the City of Adrian. Conversely, the Capital Projects Revolving Fund, Dial-A-Ride, Storm Water Utility and the Automobile Parking System funds are combined into a single, aggregated presentation in the proprietary fund financial statements. Individual fund data for these enterprise funds is provided in the form of *combining statements* elsewhere in this report. The basic proprietary fund financial statements can be found on pages 70-74 of this report.

Fiduciary Funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are *not* available to support the City of Adrian's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds.

The basic fiduciary fund financial statements can be found on page 75 of this report.

Notes to the Financial Statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 76-105 of this report.

Other Information. In addition to the basic financial statements and accompanying notes, this report also presents certain *required supplementary information* concerning the City of Adrian's progress in funding its obligation to provide pension benefits to its employees through employer contributions and required employee contributions. Required supplementary information can be found on page 107 of this report.

The combining statements referred to earlier in connection with non-major governmental funds and enterprise funds are presented immediately following the required supplementary information on pensions. Combining and individual fund statements and schedules can be found on pages 109-135 of this report.

The Schedule of Indebtedness can be found on pages 173-176.

Economic Condition Reporting: The Statistical Section

The Governmental Accounting Standards Board (GASB) has issued Statement 44 regarding Economic Condition Reporting for General Purpose Local Governments. Although the provisions of Statement 44 were effective for Statistical Sections prepared for periods beginning after June 15, 2005, the City of Adrian met the intent of this Statement through early adoption (FY2004-05) and by improving the understandability and usefulness of the Statistical Section information by addressing traditional comparability issues that have developed in practice and by adding information from the new financial reporting model for state and local governments required by Statement 34.

Statement 44 establishes the objectives of the Statistical Section and the five categories of information it contains – financial trends information, revenue capacity information, debt capacity information, demographic and economic information, and operating information.

This part of the City of Adrian's comprehensive annual financial report presents detailed information as a context for understanding what the information in the financial statements, note disclosures, and required supplementary information says about the City's overall financial health.

Financial Trends

These schedules contain trend information to help the reader understand how the City's financial performance and well-being have changed over time.

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Exhibit B-3:	Fund Balances, Governmental Funds, Last Ten Years	182
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Exhibit B-5	Program Revenues by Function/Program, Last Four Years	184
Exhibit B-6	Tax Revenues by Source-Govt'l Fund, Last Ten Years	185

Revenue Capacity

These schedules contain information to help the reader assess the City's most significant local revenue source, the property tax.

Exhibit C-1:	Assessed Value and Actual Value of Taxable Property (Last Ten Fiscal Years)	186
Exhibit C-2:	Direct and Overlapping Property Tax Rates (Last Ten Fiscal Years)	187
Exhibit C-3:	Principal Property Tax Payers (Current Year and Nine Years Ago)	188
Exhibit C-4:	Property Tax Levies and Collections (Last Ten Fiscal Years)	189

Debt Capacity

These schedules present information to help the reader assess the affordability of the City's current levels of outstanding debt and the City's ability to issue additional debt in the future.

Exhibit D-1:	Ratios of Outstanding Debt by Type (Last Ten Fiscal Years)	190
Exhibit D-2:	Ratios of General Bonded Debt Outstanding (Last Ten Fiscal Years)	191
Exhibit D-3:	Direct and Overlapping Government Activities Debt (as of June 30, 2005)	192
Exhibit D-4:	Legal Debt Margin Information (Last Ten Fiscal Years)	193
Exhibit D-5	Pledged-Revenue Coverage (Last Ten Fiscal Years)	194

Demographic and Economic Information

These schedules offer demographic and economic indicators to help the reader understand the environment within which the City's financial activities take place.

Exhibit E-1:	Demographic and Economic Statistics (Last Ten Calendar Years)	195
Exhibit E-2:	Principal Employers (Current Year and Nine Years Ago)	196

Operating Information

These schedules contain service and infrastructure data to help the reader understand how the information in the City's financial report relates to the services the City provides and the activities it performs.

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Exhibit F-2:	Operating Indicators by Function/Program (Last Ten Fiscal Years)	198
Exhibit F-3:	Capital Asset Statistics by Function/Program (Last Ten Fiscal Years)	199

Government-wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the City of Adrian, assets exceeded liabilities by \$69,435,564 at the close of the most recent fiscal year.

By far the largest portion of the City of Adrian's assets (85.0%) reflects its investment in capital assets (e.g., land, buildings, machinery and equipment), less any related debt used to acquire those assets that is still outstanding. The City of Adrian uses these capital assets to provide services to citizens; consequently, these assets are *not* available for future spending. Although the City of Adrian's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to pay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

CITY OF ADRIAN'S NET ASSETS

	Governmental Activities		Business-Type Activities		Total	
	FY2009-10	FY2008-09	FY2009-10	FY2008-09	FY2009-10	FY2008-09
Current and Other Assets	\$10,080,779	\$11,663,168	\$5,653,283	\$4,286,530	\$15,734,062	\$15,949,698
Capital Assets	34,839,240	29,271,307	55,178,378	56,828,605	90,017,618	86,099,912
Total Assets	\$44,920,019	\$40,934,475	\$60,831,661	\$61,115,135	\$105,751,680	\$102,049,610
Long-Term Liabilities	\$1,852,906	\$1,635,076	\$26,627,323	\$438,667	\$28,480,229	\$2,073,743
Other Liabilities	7,475,988	4,272,752	359,899	27,759,794	7,835,887	32,032,546
Total Liabilities	\$9,328,894	\$5,907,828	\$26,987,222	\$28,198,461	\$36,316,116	\$34,106,289
Net Assets:						
Invested in Capital Assets (Net of Related Debt)	\$27,799,240	\$25,580,401	\$29,232,995	\$29,120,469	\$57,032,235	\$54,700,870
Restricted	4,293,813	3,832,553	1,925,361	1,112,269	6,219,174	4,944,822
Unrestricted	3,498,072	5,613,693	2,686,083	2,683,936	6,184,155	8,297,629
Total Net Assets	\$35,591,125	\$35,026,647	\$33,844,439	\$32,916,674	\$69,435,564	\$67,943,321

An additional portion of the City of Adrian's net assets, nine (9.0%) percent, represents resources that are subject to external restrictions on how they may be used. The remaining balance of *unrestricted net assets* (\$6,184,155) may be used to meet the City's ongoing obligations to citizens and creditors. At the end of the current fiscal year, the City of Adrian is able to report positive balances in Net Assets for both Capital Assets and Unrestricted categories. The increase (\$1,274,352) in Restricted Assets for Governmental Activities is due to the reservation of Vibrant Small Cities Grant Funds to pay for the completion of the Two-way Traffic Conversion Project and the increase in Restricted Assets for

Business-Type Activities is due to increased coverage needed for future Utility Fund revenue bond debt service.

Change in Net Assets. As explained earlier under Financial Highlights, the City's total net assets increased by (\$1,492,243). A summary of the net increase, segregating Governmental Activities and Business-Type Activities, as well as a comparison with prior year's actual, follows: **CITY OF ADRIAN'S CHANGES IN NET ASSETS**

	Governmental Activities		Business-Type Activities		Total	
	FY2009-10	FY2008-09	FY2009-10	FY2008-09	FY2009-10	FY2008-09
Revenues:						
Program Revenues:						
Charges for Services	\$3,179,286	\$2,614,527	\$8,136,267	\$7,678,976	\$11,315,553	\$10,293,503
Operating Grants & Contributions	659,426	1,159,543	249,672	234,216	909,098	1,393,759
Capital Grants & Contributions	905,658	256,986		598,577	905,658	855,563
Total Program Revenues	\$4,744,370	\$4,031,056	\$8,385,939	\$8,511,769	\$13,130,309	\$12,542,825
General Revenues:						
Property Taxes	\$7,519,378	\$7,435,559			\$7,519,378	\$7,435,559
Other Taxes	3,307,798	3,813,969			3,307,798	3,813,969
Grants & Contributions not Restricted to Specific Programs	13,032	13,307			13,032	13,307
Other	451,469	605,702	\$345,657	\$69,753	797,126	675,455
Total General Revenues	\$11,291,677	\$11,868,537	\$345,657	\$69,753	\$11,637,334	\$11,938,290
Total Revenues	\$16,036,047	\$15,899,593	\$8,731,596	\$8,581,522	\$24,767,643	\$24,481,115
Expenses:						
General Government	\$2,309,265	\$2,964,862			\$2,309,265	\$2,964,862
Public Safety	5,152,144	4,642,682			5,152,144	4,642,682
Public Works	1,247,332	1,066,018			1,247,332	1,066,018
Culture and Recreation	3,506,682	4,263,702			3,506,682	4,263,702
Comm. Beautification & Impv. Community/Economic Development	1,208,425	2,344,407			1,208,425	2,344,407
Highways, Streets & Bridges	368,582	278,357			368,582	278,357
Interest on Long-Term Debt	1,332,172	1,141,891			1,332,172	1,141,891
Wastewater System	232,140	148,061	\$3,917,578	\$4,209,153	3,917,578	4,209,153
Water System			3,152,628	3,091,711	3,152,628	3,091,711
Dial-A-Ride System			514,754	510,315	514,754	510,315
Auto Parking System			82,711	97,254	82,711	97,254
Storm Water Utility			250,987	203,341	250,987	203,341
Total Expenses	\$15,356,742	\$16,849,980	\$7,918,658	\$8,111,774	\$23,275,400	\$24,961,754
Excess/(Deficiency) Before Transfers	\$679,305	(\$950,387)	\$812,938	\$469,748	\$1,492,243	(\$480,639)
Transfers	-114,827	-106,115	114,827	106,115	0	0
Increase/(Decrease) in Net Assets	\$564,478	(\$1,056,502)	\$927,765	\$575,863	\$1,492,243	(\$480,639)
Net Assets – Beginning	\$35,026,647	\$36,083,149	\$32,916,674	\$32,340,811	67,943,321	68,423,960
Net Assets – Ending	\$35,591,125	\$35,026,647	\$33,844,439	\$32,916,674	\$69,435,564	\$67,943,321

Financial Analysis of the Government's Funds

As noted earlier, the City of Adrian uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds. The General Fund is the chief operating fund of the City of Adrian and is considered a Governmental Fund. The focus of the City's *governmental funds* is to provide information on near-term inflows, outflows, and balances of *spendable* resources. Such information is useful in assessing the City of Adrian's financing requirements. In particular, *designated* and *unassigned General Fund - fund balance* may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year. As of the end of the current fiscal year, the City of Adrian's governmental funds reported designated and unassigned fund balance for the General Fund of \$1,712,844, a decrease of \$2,385,431 in comparison with the prior year. The primary cause for the decrease is due to the planned utilization of \$2,250,000 of Designated Fund Balance to partially defray the cost of the Downtown Government Complex Project, thereby minimizing the amount required from long-term debt financing. Nevertheless, the amount available still represents over fifteen (15.3%) percent FY2010-11 Budgeted General Fund expenditures, while total fund balance represents thirty (30%) percent of that same amount.

Other Governmental Funds include Major Streets, Local Streets, and Fee Estate Funds, as well as other minor funds, such as Perpetual Care and Endowment Funds. Collectively, their fund balances decreased by \$319,507, to \$3,906,999, primarily due to the slow reimbursement of Small Vibrant City Grant expenses from the Michigan State Housing Development Authority.

Proprietary Funds. The City of Adrian's Proprietary Funds provide the same type of information found in the government-wide financial statements, but in more detail.

Net assets of the Wastewater Fund at the end of the year amounted to \$15,653,188, an increase of \$304,473, attributable to an authorized rate increase enabling contributions to Net Assets sufficient to cover increased debt service expenses related to implementation of a Wastewater System Improvement Project Plan. The Water System experienced a \$676,646 increase in net assets, from \$12,137,445 to \$12,814,391, primarily due to increased revenue from charges for services and sale of surplus property.

All other Proprietary Funds, including Storm-Water Utility, Automobile Parking System, Dial-A-Ride System and Capital Projects Revolving Fund, experienced a collective decrease in Net Assets amounting to (\$53,654), equivalent to (1.0%). The primary contributing factor to this decrease is an increase in equipment depreciation for the Dial-A-Ride bus fleet.

General Fund Budgetary Highlights

Differences in the original budget and the final amended budget amounted to a \$2,462,063 increase in appropriations and are detailed as follows:

Downtown Gov't Complex Financing - Local Match on Debt Financing	\$2,250,000
Encumbrances & Carry Forwards	341,359
Motor Vehicle Pool Revised Revenue Estimate - 2nd Qtr Budget Amendments	290,000
3rd Qtr Budget Amendments	(\$267,222)
Revenue Sharing (Executive Order 2009-22)	(209,643)
Actual Bond Proceeds - 2nd Qtr Budget Amendments	(110,000)
Police JAG Grant	80,219
Inspection Fee Income - 2nd Qtr Budget Amendments	(59,000)
Swigert Donation - Piotter Kitchen Addition	52,930
Investment Earnings - 2nd Qtr Budget Amendments	(50,000)
Library Capital Impr. Donations	55,863
Aggressive Del Property Tax Collection	40,000
Contribution-Utilities - 2nd Qtr Budget Amendments	(40,000)
Dept on Aging Grant - Piotter Kitchen Addition	27,013
Library Penal Fines - 2nd Qtr Budget Amendments	(25,000)
State Fire Protection Payment	17,000
Park Master Plan	13,750
Library Furniture Donations	10,685
Private Donations - Cable TV	10,000
Refuse Millage Tax Receipts – 2nd Qtr Budget Amendments	8,000
Contribution-Drug Forfeiture Fund	5,000
Non-Drug Enforcement Forfeitures - Truck Axle Scales	5,000
Office of Highway Safety Program - Traffic Grant	4,211
Swigert Donation to Resurface Shuffle Boards at Piotter Center	3,800
Library Café Lease	3,960
Narcotic Enforceemnt Grant	2,216
Community Development Contribution - Cleirical Support	2,000
2nd Qtr Budget Amendments	(\$1,278)
Private Donations - Motorcycle Sponsorship	1,200
Total	<u>\$2,462,063</u>

The above listed appropriations were budgeted from available fund balance. During the year, however, expenses were less than the amended budgetary estimates, thus reducing the need to draw upon existing fund balance by \$1,208,474 to \$1,253,589. Significant variances between the Amended General Fund Budget and Actual Revenue and Expenditures are identified and explained as follows:

Revenue:

Compared to the Amended Budget, actual revenue was unfavorable by (\$3,925,859), primarily due to a planned draw down on Fund Balance for the Downtown Government Complex (\$2,250,000), Contribution of working capital to the expanded Motor Vehicle Pool (\$700,000) and renovation of the Adrian Public Library (\$600,000).

Expenditures:

Compared to the Amended Budget, actual expenditures were favorable by \$2,556,221. The primary reasons for this favorability are detailed as follows:

- 1) Police Department was favorable by \$260,465 due to Capital Improvement under-spending on new Police Facility.
- 2) Department of Public Works was favorable by \$113,912 due to postponement of Capital Improvements, replacement windows and siding, on the Public Works Building.
- 3) Parks & Forestry Division was favorable by \$344,928 due to Capital Improvement under-spending on renovation of new Parks & Forestry Maintenance Facility.
- 4) The incomplete Downtown Government Complex Project had unspent funds as of June 30 amounting to \$1,235,689.
- 5) General Fund Contingency Account ended the year with a favorable balance of \$452,195.

Capital Asset and Debt Administration

Capital Assets. The City of Adrian's investment in capital assets for its governmental and business-type activities as of June 30, 2010 amounts to \$90,017,618 (net of accumulated depreciation), representing a year-to-year increase of \$3,917,706. Governmental Activities increased \$5,567,933, from \$29,271,307 to \$34,839,240, primarily due to building acquisitions renovation and construction related to the new Downtown City Government Complex and the new Parks & Forestry Maintenance Building, as well as increase in the value of the City's infrastructure related to Road improvements for the two-way traffic conversion project. Business-Type Activities decreased \$1,650,227, from \$56,828,605 to \$55,178,378, due to sale of surplus property and increased depreciation on assets related to construction of new Sewer and Water System improvements, including the West Well-Field Water Resource, financed by low-interest loans from the State of Michigan. Investments in capital assets include land, buildings and improvements, machinery and equipment, and park facilities, as well as roads, highways and bridges, and water/wastewater infrastructure. The total increase in the City of Adrian's investment in capital assets for the current fiscal year was 4.4 percent.

A summary of the City of Adrian's Capital Assets is provided below. Additional information regarding the City of Adrian's capital assets can be found in Note 3.C. (pages 87-90) of this report.

CITY OF ADRIAN'S CAPITAL ASSETS
(net of depreciation)

	Governmental Activities		Business-Type Activities		Total	
	2010	2009	2010	2009	2010	2009
Land	\$8,305,639	\$8,305,639	\$1,385,346	\$1,385,346	\$9,690,985	\$9,690,985
Land Improvements	5,496,288	5,729,419	937,783	1,582,008	6,434,071	7,311,427
Buildings and Systems	8,867,307	3,988,819	1,308,058	1,373,271	10,175,365	5,362,090
Utility Systems	0	0	51,430,653	44,194,311	51,430,653	44,194,311
Machinery & Equipment	2,360,750	2,834,909	116,538	697,127	2,477,288	3,532,036
Infrastructure	9,809,256	8,412,521	0	0	9,809,256	8,412,521
Construction - In-Progress	0	0	0	7,596,542	0	7,596,542
Total Capital Assets	\$34,839,240	\$29,271,307	\$55,178,378	\$56,828,605	\$90,017,618	\$86,099,912

Long-Term Liabilities. At the end of the current fiscal year, the City of Adrian had total long-term liabilities of \$34,351,118, an increase of \$2,281,241 over the prior year. Of this amount, \$7,129,000 comprises debt backed by the full faith and credit of the City, an increase of \$2,742,315 due to the Issuance of Series A, B & C bonds to acquire, renovate and construct buildings for the new Downtown City Government Complex, offset by consolidation of all outstanding General Obligation Debt. Of the total outstanding debt, \$25,843,255 represents bonds secured solely by specified revenue sources (i.e., revenue bonds), a year-to-year decrease of \$1,864,882, funds used to upgrade the City's Wastewater Collection and Treatment Systems and Water Treatment and Distribution Systems. In addition, Accrued Sick and Vacation Compensation amounts to \$647,228, a decrease of \$23,606 compared to the prior year. The City recently engaged a health benefit consultant (Kapnick Insurance Company) and, as a result, is examining the possibility of changing its accrued sick & vacation policies in favor of a Paid Time-Off Policy, including short-term and long-term disability programs.

CITY OF ADRIAN'S LONG-TERM LIABILITIES
General Obligation and Revenue Bonds
Installment Purchase Obligations
Accrued Sick and Vacation

	Governmental Activities		Business-Type Activities		Total	
	2010	2009	2010	2009	2010	2009
GO Bonds	\$7,040,000	\$ 0	\$ 0	\$ 0	\$ 7,040,000	\$ 0
Land Contract/Loans	89,000	1,482,614	0	0	89,000	1,482,614
Revenue Bonds	0	0	25,843,255	27,012,358	25,843,255	27,012,358
Installment Purchase	0	2,208,292	731,635	695,779	731,635	2,904,071
Accrued Sick & Vacation	546,873	581,846	100,355	88,988	647,228	670,834
Total Long-Term Liabilities	\$7,675,873	\$ 4,272,752	\$26,675,245	\$27,797,125	\$34,351,118	\$32,069,877

On June 30, 2010, the City of Adrian had a number of debt issues outstanding. These issues consisted of general obligation debt and revenue bonds. The City has maintained an A1 bond rating from Moody's Investor Services and an A+ rating from Standard & Poor's on general obligation issues. Under current State statutes, the City's general obligation outstanding debt amount is subject to a legal limitation based on 10 percent of total assessed value of real and personal property. As of June 30, 2010 the City's net general obligation bond and installment debt of \$7,129,000 was well below the legal limit of \$45,727,304 and General Obligation debt per capita equaled \$316.90, a year-to-year increase of \$154.76.

Additional information on the City of Adrian's long-term debt can be found in Note 3.E. on pages 93-98 of this report.

Economic Factors and Next Year's Budgets and Rates

- The FY2010-11 Budget Recommendation was submitted at a time when economic conditions were deteriorating and property values in a state of decline for a third consecutive year.
- Michigan and the nation have been going through the worst economic downturn since the 1930s. The impact on state and local budgets has been unprecedented.
- The "Great Recession" officially ended June 30, 2009 and the economy has grown modestly at the rate of 1.6%, 6.0%, 3.7% and 1.6% during each of the last four quarters. Gross Domestic Product (GDP) is forecasted to grow a meager 1.3%, 1.6%, 2.3% and 2.1% during the next four quarters, with a boost to 2.7% and 3.6% in the last half of 2011.
- Although corporate profits are up sharply for 2009-2010 and over 750,000 jobs have been created since December 2009, unemployment remains at 9.6%.
- The national recession has worsened Michigan's economic woes, pushing unemployment up to 16.2 percent in July, the second highest rate in the nation after Nevada, causing residents to cut back on spending, which hurts state sales tax revenue and, in turn, State Revenue Sharing to local units of government..

All of these factors were considered in preparing the City of Adrian's budget for the 2010-11 fiscal year. Also during the current fiscal year, designated and unassigned fund balance in the General Fund stands at \$1,712,844 or just over fifteen (15.3%) percent of total general fund expenditures included in the FY2010-11 Budget. The City of Adrian has designated \$646,000 of the unassigned Fund Balance amount for spending in the ensuing fiscal year budget recommendation, primarily for the purpose of funding working capital for the proposed Office Space Rental Program. This Program will provide on-going financing of all building maintenance and operations, as well as replacement of all or parts of City facilities over time.

Building on the work an expert consultant previously engaged to perform a User Rate Analysis, including the financial impact of existing and future debt service requirements, as well as projected replacement/renovation capital projects costs, the Utility Department annually updates the analysis which is utilized to determine the ensuing year's water and sewer rates. Based on that analysis, the FY2010-11 Budget reflects a rate increase of five (5%) percent for both water and sewer services.

With a constant tax levy of 15.6039 mills (including operating, refuse collection and road improvements), good stewardship has been reflected in the management of City finances. It should be noted that the current refuse contract expires December 31, 2010 and is reflected in the FY2010-11 Budget as a fiscally unsustainable program, with revenue derived from a one mill property tax levy generating \$440,000 annually compared to a cost for this service approximating \$605,000 annually. It is anticipated that the City Commission will address this issue by examining the method and level of service provided, as well as the source of funds necessary to sustain the service into the future.

Requests for Information

This financial report is designed to provide a general overview of the City of Adrian's finances for all those with an interest in the City's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Office of the Finance Director, 135. W. Maumee Street, Adrian, Michigan 49221 or call 517-264-4824 or e-mail: jpardee@ci.adrian.mi.us